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Taxation of Mobile Capital in a Global Free Market: Opportunities and Threats for Low Tax Countries

Mason Gaffney

It has been almost a decade since the ILLINOIS REAL ESTATE LETTER last featured the views of Dr. Mason Gaffney, one of our favorite economists (see "How to Revive a Dying City," Summer 1989). We are, therefore, delighted to offer our readers Gaffney's views on taxing mobile capital. The presentation in the following pages is adapted from a speech given by Gaffney on October 21, 1998 at The Adam Smith Forum, part of the 10th Annual International Trust and Tax Planning Conference sponsored by Offshore Trust Services and held in New York.

The Organization for Economic Cooperation and Development (OECD), an association of top economic officials from many countries, tells us that international tax competition is a "harmful" activity that should be stamped out. While this warning may be merely ceremonial, I fear that it is not. When a powerful international political organization officially brands you as "harmful," look out. As Henry Clay stated in the US Senate on March 14, 1834, "The arts of Power and its minions are the same in all countries and in all ages. It marks its victim; denounces it; and excites the public odium and the public hatred, to conceal its own abuses and encroachments."

Power Plays

We learn about power plays, to our sorrow, in the academy as well. Although it is comforting to view the "ivory tower" as a place governed only by intellect, the politics can be as cannibalistic as outside. Indeed, some university administrators have proven especially adept at violating the 9th Commandment: "Thou shalt not bear false witness against thy neighbor." In the campus setting it would actually involve thy *faculty* rather than thy neighbor, but in any case the bearing of false witness is a sin so harmful that Moses ranked it right up there with theft, adultery, and even murder. Defamation anticipates oppression, conditioning suggestible minds to accept it.

The connection between academics and misguided international economic policies is that the OECD's tentacles extend deep into the scholarly world, where they get quick action. The *National Tax Journal*, a sedate scholarly outlet that should be detached from political pressures, picked up on the tax competition theme instantly. Joann Weiner of the US Treasury's Office of Tax Analysis (OTA), and Hugh Ault of the OECD (and Boston College Law School), rushed into print in the last issue an uncritical rehash of the OECD report. The normal review process is so glacial that if you discovered the meaning of life you would have to wait five years before seeing your results in print; but Weiner and Ault picked up the Report on May 1, pondered it, consulted, wrote their manuscript, had it "peer-reviewed" with breathtaking speed, and saw it published by September.

There are a few academics who do not agree that international tax competition harms the world. Indeed, economics students are not taught that those who advise people on how to minimize their tax burdens are sneaky free riders. Tax advisors also are not plaster saints, but that is another topic for another day (and we economists are not so perfect, either).

Precedents

So the OECD tells us that international tax competition – the setting of tax policies to attract economic activity from other countries' citizens – is "harmful." You can find OECD's own words in the Report of its Committee on Fiscal Affairs, *Harmful Tax Competition, An Emerging Global Issue*, which the OECD Council approved on April 9, 1998, and issued soon thereafter as a "Recommendation to the Governments of Member Countries." Anyone who can stay awake through its deadly prose will recognize an uncritical worldwide embrace of personal income taxation at high rates. You may find a readable summary in my August, 1998 response: "International Tax Competition: Harmful or Beneficial?"

The OECD ideal is tax "uniformity" among nations. This proposal has a familiar ring to any economist who follows fashions in the ideologies of public finance. In one closely analogous precedent, California pundits told us in 1969 or so that interurban tax competition was harmful, because it kept some cities from raising their sales taxes. To solve this problem, they invoked the doctrine of "uniformity:" if only every city raised the sales tax, no retailer or buyer could escape it by fleeing to a city without one. Accordingly, policy makers forced every city to impose a municipal sales tax, piggybacking on the existing state sales tax. The state collects it, and returns it to each municipality of origin. A few years later California cut its local property tax rates to 1/3 of their former level, and virtually froze assessed values (the property tax base). It replaced the funds with state subventions, financed by raising state sales and income levies, thereby taxing upward mobility, and subjecting its once-independent cities, counties, and schools to a high degree of state control.

A serious problem is that a "uniform" sales tax is *not* uniform in its effects. Retailers in rich locations can bear such a tax and survive; those in marginal locations can not. The result is especially to penalize poorer neighborhoods and communities and regions. Indeed, it will not surprise any reasonably jaded observer of state interventionism that there were unintended consequences. Interurban competition survives, but takes the new form of competing to attract shoppers (and hence sales tax revenues) by *over-zoning* for retail, and by subsidizing new retail outlets in various ways. The cities best able to subsidize retailers are those that are already richest, a result that adds to the bias against marginal locations.

A byproduct of subsidized retail competition is a retail vacancy rate approaching 33%, an enormous private and social cost in terms of misallocated resources. "When will they ever learn?" Not soon, apparently; the next step will be for the

state to preempt local zoning, centralizing more and more land use control in Sacramento, where control of public schools is already drifting.

Internal Contradictions of the OECD

Such centralized control is also the aim of the OECD campaign against tax competition. It is contradictory for those who preach competition in the private sector – what they call “liberalization” – to call for *suppressing* competition among governments, yet that is exactly what OECD is doing, in increasingly strident terms, as demonstrated below.

It is also incongruous for the OECD to fault tax havens for “distorting” world investment patterns when its own *internal* systems distort investment on a grand

What Is “Harmful”?

OECD says that a “harmful tax regime” is one that “attracts mobile activities.” Many of us, of course, see the attraction of activities that could have located elsewhere as the mark of a *good* system, a point to which we will return. First, consider in more detail what is meant by a “mobile” activity. Right away, we think of low income taxes, and low income tax is just what the OECD has in mind – page 27 of its Report cites low income taxes as offensive. OECD, and allied international organizations like the EU, also have a history of jumping any nation with a value-added tax (VAT) too low to suit them.

Another problem is that attributing the attraction of economic activity solely to low taxes is too simple a view by far.

It seems rather shabby of the few most fortunate nations to deny those with poorer natural endowments the best recourse available: attracting mobile capital through competitive tax policies.

scale. For example, page 31 of OECD’s Report brands a nation as “harmful” if it lets a person deduct costs when the corresponding income is not taxed. While this idea may sound reasonable, it should be clear that deductibility in the presence of untaxed benefits is the standard treatment of much real estate income in the US, the OECD’s largest member nation. Some costs of ownership – interest and property tax – are fully deductible. The cash flow is offset by overdepreciation until the property is sold. The resulting nominal gain then gets special treatment as a “capital gain,” often resulting in no tax at all, and at worst in a lower tax rate, at a deferred date. If the property in question is an owner-occupied residence with *curtilage* (a \$5 word meaning “yard”) and *pleasance* (a similarly valuable term for “landscaping”), or a private pleasure-ground, no matter how vastly spreading and preemptive, there is not even a nominal tax on the imputed income.

Thus, OECD members might derive some time-tested advice from Biblical scripture: “First pick the beam from thine own eye; then thou may see better to pick the mote from thy neighbor’s eye.”

There are two other ways for a country to attract mobile activities: by offering superior public services, and by a tax structure that favors mobile activities without stinting on public services. The latter end may be achieved simply through targeting taxes on *immobile* resources. Consider each of these points in more detail.

Richness of the Tax Base

A jurisdiction may enjoy both high public revenues and low tax rates if it has been favored with a high tax base. Alfred Marshall, the renowned Edwardian economist (credited with developing the well-known supply and demand curves so beloved by generations of introductory economics students), warned a century ago of the excessive *magnetism* of London and, within Greater London, of the richer suburbs. By magnetism, I refer to the tendency to draw economic activity that would otherwise have benefited other areas. Vancouver, BC is another example of Marshall’s principle; it is such a magnet for Canadians that the provincial government deliberately fosters developments elsewhere in British Columbia at the expense of Vancouver.

The entire province of Alberta is another such magnet, thanks to its monopoly over petroleum production in Canada, and its effective system of raising provincial revenues therefrom. The state of Alaska is another magnet; it has the highest taxes per capita of any US state, but they are paid mainly by a handful of giant oil companies with favorable leases on state-owned lands. Alaska’s magnetism takes the very direct form of an annual “social dividend” of more than \$1,000, paid in cash, for every resident of the state, adult or child. More generally, though, the whole world is divided among tax jurisdictions with richer and leaner tax bases, ranging along a wide continuum.

Note that in all those cases, the offensive “distortion” alleged to be caused by high public revenues is in *attracting* mobile factors, not in *repelling* them. The ability to attract economic activity is an advantage enjoyed by the major OECD nations, vis-a-vis those less favored by nature, by virtue of occupying the most favorable locations on the planet. It seems rather shabby of these fortunate few to deny nations with poorer natural endowments the best recourse available. If anything, the situation calls for helping poorer nations to *create* advantages.

Poorer nations may replicate the magnetism given by natural advantages, and attract mobile activities, in two ways. One is by maintaining a more efficient government: one that provides more service at a lower cost. This result is the one that competition is *supposed* to achieve in the private sector; why not in the public sector, as well? The other way is by adopting a magnetic tax structure. There are taxes, and then there are taxes. The OECD Report was written by people wearing blinders that kept their eyes and minds glued only on the kinds of taxes that penalize and repel mobile activities. But we can liberate ourselves from that fixation. Indeed, there are taxes that do not repel mobile factors, but positively attract them; implementing them is the way to engage in beneficial tax competition. OECD ignores the potential for competition, and apparently bids us to ignore it, too, for competition will embarrass the countries that have repressive and repellent tax structures.

Magnetic Tax Structures

The US is a great laboratory for testing tax structures. It contains 51 or more separate systems, with free migration of labor and capital guaranteed by the Constitution. An example is California, whose extraordinary growth from about 1900 to 1976 shook and recast the US economy, and parts of the whole world. It was done not with low taxes and skimpy public services, but rather was, in part, the product of a tax structure that was magnetic (compared with those of other states). California's mixed bag of natural advantages did not promote much growth after the Gold Rush and the Civil War; in fact, the state's growth lagged badly for 20 years or more. Eventually, though, growth-oriented forces prevailed. The state provided superior public services of many kinds: water supply, schools (even the public universities were tuition-free), health services, transportation, parks and recreation, and others. The state held utility rates down by regulation, while resisting the temptation to overtax the utilities.

Of course, all that service required tax revenues, and a conducive tax base. California had oil, but did not tax its extraction, and still does not. The state's wine industry also has gone virtually untaxed. There was, and still is, hardly any tax on California's magnificent redwood timber, either in the cutting or in letting it stand. There was no charge for using falling water to generate electric power, or for withdrawing water to irrigate the desert areas. Most of those activities could have provided suitable tax bases, but California wisely chose to follow a different path in raising revenues for the public coffers.

Its main tax source was another kind of immobile resource: ordinary real estate. In fact, California's tax valuers focused their attention on the *most* immobile *part* of real estate, the land, such that by 1918 land value comprised 70% of the state's property tax base. In addition, there were special assessments on land. Yet people and capital flooded in; labor and its tools are mobile in response to opportunities. California became the most populous state, and the largest (or at least a major) producer of many things, from farm products to the "tertiary" services of banking, finance, and insurance.

Competition is Not Harmful

Was California's attempt to compete by enacting favorable tax policies harmful? On the contrary, in a world of self-aggrandizing governments, intergovernmental competition is the only thing that makes life bearable. It is true that competition from nations or cities with rich tax bases can distort the allocation of mobile factors, but mobile factors are not what OECD is targeting. Rather, it is targeting the magnetic tax structures of governments that are efficient and economical.

If California's competition were harmful to the world as a whole, we would have to conclude, by analogy, that the discovery of the New World was harmful, too: Columbus should have stayed home. While it is "politically

era "Okies" been forced to remain in the Dust Bowl instead of finding new lives in California. Even the *braceros*, Hispanic "guest-workers" who toil in the fields, send money home, relieving problems in their homelands. What is involved in these cases, in spite of some well publicized abuses, is turning those who would have few opportunities in their home areas into highly productive people.

But labor has not been the only beneficiary; California offered a higher return on capital, too. For example, there emerged the "continental tilt" of interest rates," higher in the west to overcome the frictions of space and draw eastern capital to where it was more welcome. Over time, buildings that wore out in the east were replaced in California.

OECD ignores the potential for competition among tax regimes, and apparently bids us to ignore it, too, for competition will embarrass nations with repressive and repellent tax structures.

correct" today to stress the negative side of the migration of Europeans and their capital to the New World, I doubt if many people, on balance, would be better off in a world shrunk to its Eastern Hemisphere.

California became the largest producer of cotton, for example, displacing a good deal of cotton from traditional southern state producers. Yet the damage to those producers was offset by an equal gain to cotton buyers, with a net gain from higher usage due to the lower price. Marginal cotton fields were released for other uses, like reforestation. (I must concede that California's success could have been due, in part, to subsidies, and to racing for cotton quotas during the Korean War; there are few pure examples of anything in this complex world.)

California also attracted workers from the eastern US, tending, in the process, to pull up eastern wage rates. The damage to eastern employers was offset by an equal gain to their workers, with large net gains from two sources. One was a more equal distribution of wealth; the other was a drop in welfare costs, and in social problems. For example, more crime would likely have ensued had depression-

Did California's vigor seem too ambitious, so as to damage others? If so, as Marc Antony said, "it were a grievous fault," apparently worthy of suppression by the OECD. Most economists believe, though, that investing is the motor that drives prosperity, and raising investment opportunities is the key to the motor; I certainly agree. OECD does not, it seems, for last July it pressured Spain, an emerging member, to reduce its interest rates to the "Euro convergence rate" of 3.5%. Any nation pursuing "harmful tax policies" to raise investment opportunities would upset some delicate balance or grand plan, it seems.

When California competition pulled up interest rates back east, some borrowers were hurt. These losses, however, were offset by equal gains to savers, with a net bonus from the rise in saving caused by higher interest rates. There are those who would intuitively assume that the distributive effects are regressive, but that is doubtful. In this case, the truth is counter-intuitive. Note that equity *earnings* in stocks and real estate vary inversely with interest rates. Equity *values* are impacted even more, because

higher interest rates translate into higher capitalization rates, which mean lower price-to-earnings (P/E) ratios and lower capital gains.

This issue is too big to settle in a few words, but on balance, in my view, a rise in interest rates has an equalizing effect on the distribution of wealth, all the more so when the initiating cause is an expanded choice of investment outlets. The net "micro," or allocative, effect of higher rates is to move capital to higher uses, as corporate directors impose higher hurdle rates on their managers. (A *hurdle* rate is a minimum acceptable rate of return on a prospective investment.) Hurdle rates rose, not because there was less capital overall, but because there were more opportunities to invest capital productively.

Proposition 13 capped property taxes, but raised the taxes that "shoot anything that moves." The result has been an "Alabamization" of California schools and the largest prison population of any state.

Basically, California's remarkable 20th Century growth extended our American tradition of the western frontier, in the spirit of Thomas Jefferson, as a "safety valve" for mobile resources oppressed in the older states. It limited the power of the "haves" over the "have-nots," with net gains all around. Was this impressive growth the product of untaxing wealth, and dumping taxes on poor workers and consumers? The OECD says that competition is harmful because it limits the power of OECD nations to tax "wealth," thus more-than-intimating that it is upholding the interests of labor. The premise, at least the one OECD states, is that wealth is more mobile than labor. But California relied on the property tax, and recall that 70% of the tax base was pure land, totally immobile. OECD treats land like one of those unmentionable four-letter words.

Was California growth simply the product of southwestern pioneer vigor? Compare California with New Mexico, a Third World nation masquerading as our 47th state. Since before statehood, an oligarchy of giant landowners, in the million acre class, has dominated the

political apparatus; members have used their power to keep taxes off their vast lands. New Mexico raises a lower fraction of its state and local revenues from the property tax than does any other state. Its economic base, to the extent that an economic base exists, is mainly the product of what Senator Albert Beveridge of Indiana called "the free coinage of western Senators." New Mexico gets more federal spending per capita than almost any other state, but federal largesse and scenery are about the only means of raising revenues. Boosters call it *The Land of Enchantment*, but The Enchanter has cast a sleeping spell on all local enterprise. New Mexico has the highest poverty rate in the United States and, in its wide open spaces, a very high rate of violent death.

Changes for the Worse

In 1978, California took a giant step backwards by enacting its "Proposition 13," capping property tax rates at about a third of their previous level. The national ranking of the state's services began a precipitous fall; so did the per-capita income. Struggling to maintain itself, California has raised sales, income, and business taxes to unprecedented levels. These kinds of taxes "shoot anything that moves," while sparing immobile resources that do not. The result has been a rapid "Alabamization" of California, as the Golden State has fallen to join the state with the worst school system in the nation. Immigration has changed to outmigration, and among those who stay, California has by far the largest prison population of any state – so large that the union of prison guards is now our most powerful lobby, and building prisons is our fastest growing construction industry. None of the directly involved people, prisoners or prison builders or guards, are producing goods and services for others. Thus, even with all the employment in the prison sector, California's unemployment rate is above the national average.

Today, if we look for a new frontier – in terms of taxes – we find it in, of all places, one of the original 13 colonies. New Hampshire, with its poor soils, marshy peneplains, harsh climate, impassable mountains, and lack of natural urban confluences, now has the least repellent tax structure in the nation. The *Live Free or Die* state does not tax sales or personal income, while two thirds of all its state and local revenue comes from the property tax. The state has bucked the national trend toward taxing income and sales, and *it has prospered!* (Details can be found in a chapter that Richard Noyes and I wrote for *The Losses of Nations*, edited by Fred Harrison, 1998.)

Why Tax Competition Is Beneficial

A more efficient government would offer superior public services without higher taxes, or the same services with lower taxes. Is this outcome harmful? Those who sanction competition in business as a means of attracting suppliers and customers (thereby placing market discipline on private enterprise and undercutting monopolies) should, by the same reasoning, also endorse competition among *governments* to attract people and capital. This type of competition is a major defense against the tyranny that a monopoly government can exercise.

Every government has some latent monopoly power by its nature. Specifically, government has a monopoly of power over the land within its jurisdiction. Governments would like, especially, to attract and retain industries in their jurisdictions that are clean, safe, and generative of fiscal surpluses; service industries provide a noteworthy example. Through supporting the OECD efforts to stifle competition, governments will fight to keep these activities from migrating elsewhere. As Baroness Symons, a high-ranking UK treasury official, remarked recently, London itself is the largest "offshore" financial center.

The benefits of intergovernmental competition are exemplified by Europe in the 16th Century, an age of nation building that also saw a worsening in returns to the mobile factor, labor. Before that time, during the anarchic Wars of the Roses in England, for example, dozens of petty tyrants competed to hold on to their

retainers and archers, making the 14th and 15th Centuries a golden age for English labor. Competition tempers tyranny. Economic historians have shown that living standards for workers in this golden age were higher than in the 19th Century, despite all the latter period's technical progress. (The Church used its vast land holdings to provide the medieval welfare system.) But Tudor monarchs then put an end to such wasteful competition among tyrants. They let their favorites enclose the commons, and replace people with sheep. Thousands were cast loose to roam as "sturdy beggars," and then whipped back, landless and desperate, to serve on the masters' terms. Thus was the modern age born in an agony brought on by ending competition among governments.

Should All Tax Regimes Be the Same?

Uniform taxation does *not* produce uniform results, a phenomenon that economists acknowledge in their theorizing as the "Ramsey Rule" (after 1920s Oxford economist Frank P. Ramsey). Yet having nodded to this result in theory, many of these economists then pass over it in prescribing actual tax policy – a maddening ambivalence that I deplore, but will not try to explain here. Economists would improve their policy prescriptions if they gave more weight to the Ramsey Rule. In some disfavored regions, or "lean territories" at the edges of settlement, the land generates little or no surplus above the opportunity cost of the mobile factors. Labor just makes wages; capital earns only enough to pay interest. Imposing a uniform general sales tax (GST), pay-as-you-earn (PAYE) tax, or VAT makes economic life nonviable at these lean edges, because there is no taxable surplus there; you can not get blood from a stone.

For example, in South Africa a VAT was imposed with the very purpose of extracting taxes from the poor black residents in the Backveld regions. The result was to sterilize the Backveld economically, scorch the earth, and drive people away to squat in extra-legal shantytowns like Soweto near Johannesburg, and The Crossroads near Cape Town. It forced these people to survive by hawking in gray markets on the streets and roadsides, turning also to drugs, prostitution, and crime. What else could they do?

A place as rich as Vancouver might impose a VAT and survive, but it is not clear that it should. Hong Kong is the sparkling paragon of a rich territory that embraced magnetic tax policies. As a UK colony, it redoubled its natural magnetism by shunning repellent taxes of most kinds. Its public coffers overflowed, nonetheless, because the Crown owned all the land, and did a better than average job of collecting much of the surplus for public purposes. With a tiny land area, Hong Kong became a world center of both secondary and tertiary industry, with a large population and a high per capita income by world standards. Those who have eyes to see, let them see.

National governments not owning their own land can replicate the Hong Kong effect simply by emulating California of yesterday, and New Hampshire of today, basing most of their taxes on the immobile factor, land. Tax capital and capital flight is a hazard, but land never flies nor flees. Tax labor and brain-drains become a menace, but land stays home.

Choices for OECD Nations

If OECD nations worry about tax competition, they have at least three choices:

A: They can impose exchange controls to prevent capital export, as attempted by various authoritarian states before World War II, and by some welfare states since then. This approach had its day, and is now a proven failure, although that is not stopping some desperate failing Asian nations now from giving it another whirl.

B: They can muscle small nations into creating, and help them to enforce, their own repressive tax systems. This choice requires extending OECD sovereignty worldwide, as envisioned in the OECD Report. Greater OECD power is in the spirit of the times, in an age of world cartels, multinational corporations (MNCs), the International Telecommunications Union, world radio and TV networks, the IMF, the World Bank, the World Trade Organization (WTO), the MAI (not a real estate appraiser, but rather the Multilateral Agreement on Investments, another OECD boon), the Trilateral Commission, Interpol, the world war on drugs, the US as world policeman, *etc.* It is something like the Holy Alliance

that undertook to police aberrant nations of post-Napoleonic Europe, only more ambitious, with a worldwide turf and no exceptions or refuges. Any independent force threatens the whole structure, so it demands nothing short of the megalomaniac goal of worldwide domination.

The megalomaniac mindset is seen in a recent statement from Italian Treasury Minister Carlo Ciampi that the IMF's interim committee must become "the embryo" of an economic government for the world. His view backs last April's call by IMF Managing Director Michel Camdessus for the interim council to become a body producing binding directives rather than recommendations. The UK's Baroness Symons made it even plainer in a September 1998 address, telling us that the new OECD guidelines are intended not just for members and their territories, but "non-members as well. It is, therefore, an ambitious attempt to create a new international standard to apply equally to all jurisdictions."

C. They could reform their own domestic tax systems along the lines demonstrated by California before 1978, by Hong Kong before 1997, and by New Hampshire today. They could lead us to a world of benign tax competition. They could move away from extra-territorial taxation to purely intra-territorial taxation; away from taxing people toward taxing things; and away from a mobile tax base toward a more immobile tax base. Of course, these countries are not headed in those directions today, but if one or two nations can face OECD down and set the right examples, others will have no choice but to follow suit. Freedom anywhere foils tyranny everywhere. Tax tyranny is a balloon: seal every leak, or it collapses.

A World Network for Tax Intelligence

A related OECD concern is extending the sovereign powers of its members to pry into private dealings in *other* nations. The French verb *percevoir* has two meanings: "to perceive" and "to tax;" how clever of the French to have noticed that connection. To tax something, you must first conceive it and see it. Indeed, income tax agents are necessarily *voyeurs*. They are frustrated and offended by privacy provisions in other nations and, as the OECD Report makes clear, they believe they

have the moral authority to pierce those veils, and to invoke political force for what they see as a just purpose.

Must it be so; is taxation always at war with personal privacy and national sovereignty? Fortunately, the answer is no. The OECD Report tacitly premises that all taxes must be on a personal (or corporate) basis, what the lawyers call *in personam*. Some other taxes, however, are levied on things, or *in rem*. Import duties, for example, are levied on dutiable goods brought in, regardless of by whom or where from (though sometimes the latter question is considered). No inquisition is needed into the personal affairs of the importer. Enforcement consists simply of refusing to admit the goods until the duties are paid or, in extreme cases, seizing the goods. Only in criminal cases are the people involved penalized or jailed. Yet there are upper limits on feasible tariff rates, and many national borders are long and penetrable. In fact, many nations are lowering (or eliminating) import duties in the interests of freer world trade, another strong trend of the times. Many groups rebel against high domestic consumer prices, as well. The weight of opinion thus is that import duties, and all such consumer taxes, are regressive and socially undesirable.

A purer case of *in rem* taxation is the tax on real estate. Such taxes are liens on land, not on land owners. Sovereignty over land is unambiguous; a parcel is either inside or outside the taxing jurisdiction, regardless of who owns it, where the owner resides, what other assets he or she may own, or other income he or she may receive in or outside the jurisdiction. No international tax treaties are needed in order for a nation, or smaller jurisdiction, to tax land within its borders. No information need be demanded of any other nation or its institutions, as a rule. The important exception is a severance tax on minerals exported by MNCs that use internal pricing to transfer profits to low-tax jurisdictions – a case calling for drastic remedies on the home front.

Adam Smith wrote in 1776 that if you tax stock (movable capital) it will be concealed or removed. Worse, some forms of capital are more concealable and removable than others, so a tax on capital, even on *all* capital, is necessarily nonuniform.

Knowing the quantity of mobile capital requires a deep inquisition “as no people could support” (*Wealth of Nations*, page 800). Capital is never uniformly taxed, and never can be, even within one nation. In today’s world economy, with instant electronic encrypted international fund transfers, the ability of creative people to legally avoid or illegally evade taxes on mobile capital has outrun even Smith’s pioneering insights.

The OECD’s response has been to call for more enforcement, and to scapegoat small tax havens. Yet enforcing income taxes today calls for nothing less than a worldwide intelligence network with vast powers of search and seizure. It also calls for worldwide thought control to give it moral authority and general support. The logical endpoint of this thought control is to criminalize income. Since that end is too absurd to proclaim in so many words, OECD nations add a step: it is not a crime to *earn* income, but it is criminal to do so without “admitting” it, and paying the prescribed civil fine. People’s minds have been conditioned to tar any failure to declare income as “cheating,” as if it were a kind of moral lapse. The OECD Report is the latest move in a long-time thought control campaign to universalize that attitude toward income. Yet because income is earned mainly through the production of goods and services, this mindset is massively counterproductive. Moreover, imposing a false, self-serving “morality” is the worst kind of immorality.

Some Final Thoughts

We have come a long way since Adam Smith gave people credit for not supporting deep inquisitions into their affairs. How he would boggle at the inquisitions tolerated today! However, now it has become clear that income taxation can not endure without a worldwide intelligence network, a worldwide inquisition by the revenue agents of every nation into the records of every other nation. Here, I submit, is where to draw the line. Here is where a determined small community, jealous and precious of its sovereignty, can defy, puncture, and collapse a bloated world tyranny. It has been done before. ■

Dr. Gaffney is a Professor of Economics at the University of California-Riverside.

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